Tax Supported
New Issue

Los Angeles County, California

Ratings

New Issues

2011–2012 Tax and Revenue Anticipation Bonds, Series A–C	F1+
Implied General Obligation Bonds	AA–

See page 2 for Outstanding Debt.

Rating Outlook

Stable

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New Issue Details

Sale Information: Up to $1,500,000,000 2011–2012 Tax and Revenue Anticipation Bonds, Series A–C the week of June 13 via negotiation.
Security: Unrestricted general fund revenue received in fiscal 2012, including requirements to set aside the first such funds received during specified time periods for note repayment.
Purpose: Provide moneys to help meet fiscal 2012 general fund expenditures.
Final Maturity: Series A notes: Feb. 29, 2012; series B notes: March 30, 2012; series C notes: June 20, 2012.

Related Research

For information on Build America Bonds, visit www.fitchratings.com/BABs.

Applicable Criteria

- *Tax-Supported Rating Criteria, Aug. 16, 2010*
- *U.S. Local Government Tax-Supported Rating Criteria, Oct. 8, 2010*

Other Research

- *Los Angeles County Public Works Financing Authority, California, Oct. 26, 2010*
- *Fitch Rates Los Angeles County, CA's $1.5B TRANs 'F1+'; Affirms Lease Ratings at 'A+' and 'A', June 9, 2010*

Rating Rationale

- Los Angeles County's projected cash flow provides strong coverage of periodic note set-asides by the pledged first dollars received, as well as after monthly expenditures when borrowable resources are included.
- The county has vast, court-verified borrowable resources available for use by the general fund.
- The note repayment structure is strong, using periodic set-asides with full principal and interest restricted well in advance of note maturity.
- As in previous years, the state's fiscal imbalance presents some uncertainty regarding the upcoming fiscal year's budget and cash flow.
- The county's vast economy is diverse and mature, with evident cyclical vulnerability.
- Financial operations are well managed with significant reserves, and the five-year extension of the federal section 1115 waiver should somewhat alleviate the pressure placed on the general fund by the Department of Health Services' (DHS) structural deficit.
- Nevertheless, finances remain vulnerable to state funding reductions, realignment of potentially underfunded state functions to the county, and heavy social service expenditures.
- While the county has a low net direct debt burden, it also has heavy investment losses to absorb in its pension system, a costly retiree medical program, and a large other post-employment benefits (OPEB) unfunded accrued actuarial liability.

Key Rating Drivers

- Strong note principal and interest coverage by pledged revenue, and by month-end cash balances when including borrowable resources.
- Full note principal and interest set-aside well in advance of note maturity.
- Continuation of good management practices, including retaining a sound general fund balance, thereby enabling the county to handle upcoming fiscal challenges.
- Ability to achieve long-term fiscal balance at the county's DHS, with permanent solutions and affordable general fund support.
- Development of an affordable plan to handle the sizable OPEB liability.

Credit Summary

Fitch Ratings' 'F1+' rating reflects the sound note repayment structure, strong coverage of all note repayment set-asides when borrowable funds are included, and the large size of the borrowable resources relative to the set-aside amounts. The repayment deposit structure sets aside 100% of principal and interest well in advance of each note maturity.

Rating History — TRANs

Rating	Action	Outlook/ Watch	Date
F1+	Assigned	—	6/9/11

Rating History — Implied GO Bonds

Rating	Action	Outlook/ Watch	Date
AA–	Assigned	Stable	6/9/11

Rating History — COPs and Lease Revenue Bonds (County)

Rating	Action	Outlook/ Watch	Date
A+	Affirmed	Stable	6/9/11
A+	Revised	Stable	4/30/10
A	Affirmed	Stable	7/29/04
A	Upgraded	—	5/23/00
A–	Downgraded	—	6/21/95
A+	Assigned	—	1/14/93

Rating History — COPs (Department of Public Social Services Facility)

Rating	Action	Outlook/ Watch	Date
A	Affirmed	Stable	6/9/11
A	Revised	Stable	4/30/10
A–	Upgraded	Stable	1/16/04
BBB+	Assigned	—	12/30/98

Outstanding Debt

Los Angeles County	
Certificates of Participation, Series 1993 Disney Parking Project	A+
Los Angeles County Capital Asset Leasing Corporation	
Edmund D. Edelman Children's Court Lease Revenue Bonds, Series 2002A	A+
Lease Revenue Bonds (LAC-CAL Equipment Program), Series 2009A	A+
Los Angeles County Public Works Financing Authority	
Lease Revenue Bonds, Series 2005 (Calabasas Landfill Project)	A+
Lease Revenue Bonds (Multiple Capital Projects I), 2010 Series A (Tax-Exempt) and Series B (Build America Bonds/Recovery Zone Economic Development Bonds)	A+
City of Los Angeles (Exposition Park West Asset Leasing Corporation)	
Certificates of Participation, Series 1999A and 1999B (Department of Public Social Services Facility)	A
Sonnenblick-Del Rio El Monte Asset Leasing Corporation	
Senior Certificates of Participation, Series 1999 (Department of Public Social Services Facility)	A
Senior Certificates of Participation, Series 2001 (Department of Public Social Services Facility — Phase II)	A
Sonnenblick-Del Rio West Los Angeles Leasing Corporation	
Senior Certificates of Participation, Series 2000 (Department of Public Social Services Facility)	A

The notes are secured by a first lien on unrestricted revenue received between December 2011 and April 2012 (projected $6.6 billion), which is projected to cover note principal and interest 4.3x. Funds for repayment will be set aside based on an aggressive schedule beginning in December 2011. By February 2012, 75% of the estimated principal and 100% of the estimated interest due will be impounded; the full amount will be set aside by April 2012. The projected cash flow covers all five set-asides well when the county's vast borrowable resources are included. However, Fitch notes that the fiscal 2012 projected cash flow remains weaker than in past years, mostly reflecting fund balance reductions and ongoing large loans to DHS to compensate for delayed state reimbursements. The county estimates that it will end six months with negative cash balances, requiring large intrafund borrowings. The county's pool of resources available for intrafund loans is projected to average $2.3 billion on a daily basis. While the county currently projects that it will require $221 million in intrafund borrowings to ensure a positive cash balance at June 30, 2012, Fitch notes that the county has a long history of outperforming its initial cash flow projections, and that about one-third of the borrowable cash is later allocated to the general fund.

The projected cash flow is based on the county's fiscal 2012 budget, which does not incorporate the state's May revised budget proposals, which are not expected to impact the general fund significantly. The county's cash flow, when borrowable funds are included, holds up well to severe stress scenarios. The county expects that it will not backfill state services that are reduced or eliminated, in line with its customary practice.

The 'F1+' rating also reflects the county's long-term credit quality. The implied GO rating of 'AA–' reflects the county's diverse and mature economy, sound financial reserves, prudent management efforts to achieve fiscal balance, and low direct debt burden balanced by ongoing and sizable financial pressures. These pressures stem from: a heavy social service spending burden, coupled with ongoing state funding uncertainty; the continued fiscal imbalance in the county's DHS; and a costly retiree medical program. Nonetheless, the county's reserve levels remain above average, providing a needed financial cushion, and DHS pressures are being partially alleviated by the five-year extension of the federal section 1115 waiver.

Economic indicators show the recession's impact, including stubbornly high unemployment at 12.2% in March 2011 for the county, down only marginally from 12.4% in March 2010. While the residential property market is showing signs of stabilizing, the nonresidential property market continues to decline. However, due to the county's highly developed and mature nature, assessed value losses have been relatively low at a 0.5% decrease for fiscal 2010 and a 1.9% decrease for fiscal 2011, indicating a significant Proposition 13 cushion. The county assessor is projecting an approximately 1% TAV increase in fiscal 2012.

While the general fund continues to generate operating surpluses, building up a sizable general fund balance, the county had a moderate net deficit in fiscal 2010 for the second consecutive year. As a result, its fiscal 2010 unreserved general fund balance decreased to $2.2 billion (15.8% of spending) from $2.6 billion (18.7% of spending) the year prior. Further erosion is anticipated at fiscal 2011 year-end, due to one-time budget solutions, with a projected unreserved general fund balance of at least $1.6 billion. Nevertheless, the county expects that its two main reserves, the rainy day fund reserve ($93.2 million) and the provisional financing uses economic reserve ($82.9 million), will remain at current levels through fiscal 2012. The county intends to increase these reserves once the economy and budget situation improve.

Despite anticipated slight revenue increases from property tax, sales tax, and vehicle licensing fees, the fiscal 2012 budget has to solve a $221 million general fund gap with a fourth year of departmental curtailments and consolidations (16%) and one-time solutions such as transferred capital program funds and a retiree health insurance premium refund (84%). From fiscal 2012 onwards, the county budget will benefit from the freeing up of $372 million annually since the county's pension obligation bonds finally mature in fiscal 2011.

The county continues to focus on the need to achieve fiscal balance in its health delivery system, given its historical reliance on significant general fund support ($750 million in fiscal 2010) and advances (approximately $1 billion outstanding) and the difficulty of reducing spending due to the size of the population served, its significant medical needs, and overcapacity. DHS's medium-term financial balance has been improved significantly by a new section 1115 waiver permitting the federal government to provide matching grants for Medi-Cal services that would otherwise be ineligible. This waiver, worth approximately $300 million per year, is effective through Oct. 31, 2015 and represents more predictable cash flows. It will assist the county in bridging the gap until federal healthcare reform is implemented in fiscal 2014 by expanding coverage, improving the payor mix, and providing new funding for system improvements. For fiscal 2012, it does not completely resolve the projected DHS deficit, so DHS needs to achieve $136 million in cost savings and/or additional revenue generation.

The county's other sizable financial challenge relates to its unfunded pension and OPEB liabilities. As of June 30, 2010 the county's pension unfunded actuarial accrued liability was $7.8 billion, due to heavy investment losses in fiscal 2009, and the funded ratio was 83%. While a further $6.2 billion of deferred investment losses will be recognized over the next three fiscal years, these should be partially offset by recent improved investment returns. Nonetheless, the county's cash contributions to its pension system continue to grow, to a projected $1.1 billion in fiscal 2012, compared to $803 million in fiscal 2010. Due to the county's conservative pension benefits structure, no new cost containment initiatives are being discussed for the county's pension system. The county also has a $22.9 billion liability for OPEB, which it is beginning to address. The county is in the process of establishing an OPEB trust, using about $470 million in excess pension fund earnings and $17 million set aside in fiscal 2007. With the county's annually required OPEB contribution estimated at $1.8 billion, more than four times the current pay-as-you-go expense, Fitch views the OPEB funding effort as important to the county's long-term fiscal stability.

The net direct debt burden is low at $150 per capita and 0.1% of market valuation. Including overlapping debt, the debt burden is a moderate $3,354 per capita and 2.9% of market valuation. Debt amortization is above-average at 78.6% retiring in 10 years.

The 'A+' ratings for the above-listed certificates of participation and lease revenue bonds reflect that their securities, county lease payments, are subject to annual appropriation and abatement. The 'A' ratings for those certificates of participation issued to fund construction of public social services facilities reflect added non-appropriation risk, since the county will not own those facilities upon lease maturity.